

Exhibit WM-3

THE COMMONWEALTH OF MASSACHUSETTS

BEFORE THE

DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

WESTERN MASSACHUSETTS ELECTRIC COMPANY

D. T. E. 00-40

PETITION for THE Issuance of ELECTRIC Rate Reduction Bonds

DIRECT TESTIMONY OF

RANDY A. SHOOP

ON BEHALF OF

WESTERN MASSACHUSETTS ELECTRIC COMPANY

April 18, 2000

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I. INTRODUCTION

Q. Please state your name and company affiliation.

A. My name is Randy A. Shoop. I am Assistant Treasurer - Finance for Northeast Utilities ("NU") including the following NU operating companies and affiliates: Western Massachusetts Electric Company ("WMECO" or "Company"), Public Service Company of New Hampshire ("PSNH"), and North Atlantic Energy Corporation ("NAEC"). I am also the Treasurer of The Connecticut Light and Power Company ("CL&P"). I am providing this testimony on behalf of WMECO. My business address is 107 Selden Street, Berlin, Connecticut.

Q. What are your responsibilities with respect to WMECO?

A. I manage the Finance Group in WMECO's Treasury Department, which is responsible for raising the capital necessary to meet WMECO's long-term and short-term financial requirements, including the issuance of electric rate reduction bonds ("RRBs"), first mortgage bonds, pollution control revenue bonds, notes, lease obligations, preferred equity, common equity and short-term bank notes.

Q: Have you previously testified in utility regulatory proceedings?

A: Yes, I have testified on behalf of WMECO before the Department of Telecommunications and Energy ("Department") regarding the issuance of debt securities. I have also testified on behalf of the other NU companies in Connecticut and New Hampshire.

II. PURPOSE OF TESTIMONY

Q: What is the purpose of your testimony?

A: My testimony will principally cover two areas. First, in order for the RRB transaction described in the Petition to proceed efficiently, waivers from certain statutory requirements regarding competitive bidding and issuance pricing must be obtained. My testimony will describe these waivers and explain why WMECO believes they should be granted by the Department.

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Second, in order to be eligible for securitization, G.L. c.164, §1G(d)(4) requires a company, inter alia, to establish an order of preference for the use of bond proceeds such that transition costs having the greatest impact on customer rates will be the first to be reduced by the bond proceeds. My testimony will describe the use of proceeds directly related to the retirement of capital and the premiums on the retirement of such capital and will explain why such use is expected to produce savings, all of which will inure to the benefit of customers.

Q. Are the proceeds of the RRB issuance expected to be applied entirely to the retirement of capital?

A. No. Proceeds of the issuance of the RRBs will also be applied to the costs of issuing the RRBs and the buyout of WMECO's remaining independent power producer ("IPP") contract. The IPP buyout is addressed in Exhibit WM-2, Testimony of Richard A. Soderman ("Soderman Testimony"). The costs of issuing the RRBs are discussed in Exhibit WM-4, Testimony of Mark A. Englander ("Englander Testimony").

III. STATUTORY WAIVERS

Q. Please discuss the statutory waivers WMECO is seeking in order to issue the RRBs.

A. WMECO seeks waivers from two Massachusetts statutory requirements. The first, G.L. c. 164, § 15, requires solicitation of competitive purchase proposals in the issuance of securities in excess of \$1 million with a life of more than five years. The second, G.L. c. 164, § 15A, requires securities to be issued at par value.

Q. Why is the Company seeking waivers from these statutory requirements?

A. Waiver of G.L. c. 164, § 15 is sought due to the significantly more complex nature of an RRB transaction as opposed to the ordinary issuance of long-term debt by a utility. This complexity requires the focused attention of a single lead underwriter for efficient and cost-effective marketing and execution of the issuance. In addition, the number of firms which have experience in the issuance of electric utility RRBs is relatively small. Under these circumstances, proceeding with a negotiated transaction instead of competitive bidding is likely to be the most efficient, least costly option, and would therefore be in the public interest.

With respect to G.L. c. 164, § 15A, the Company is seeking a waiver to enable the issuance of the RRBs at a value which may be lower than par value. The yield of these securities to the purchasers is a combination of the interest rate on the RRBs and the price at which they are sold. Market convention normally sells bonds and uses interest rates quoted in even fractions. The rate demanded by the market may not precisely match such a convention. The ability to issue bonds at a rate lower than par value will possibly enable the Company to obtain a better all-in effective cost. In a transaction of this magnitude and complexity, the flexibility to take advantage of these opportunities is likely to produce a lower cost to customers. A waiver of the G.L. c. 164, § 15A requirement so that the RRBs can be sold at less than par would therefore be in the public interest.

Q. Have such waivers been granted before?

A. Yes. WMECO has obtained such waivers on several occasions. See, e.g., D.P.U. 96-96, (March 21, 1997), waiving the two requirements in the issuance of \$60 million of first mortgage bonds. Similar waivers were also granted to Boston Edison Company ("BECO") in its securitization proceeding, D.T.E. 98-118.

IV. RETIRING CAPITAL

Q. What is the composition of WMECO's capital structure, as measured by credit rating agencies, expected to be immediately before securitization?

A. The composition of WMECO's capital structure immediately before securitization (estimated as of June 30, 2000) is expected to be as follows:

TABLE 1

PROJECTED CAPITAL STRUCTURE

JUNE 30, 2000

(Dollars in Thousands)

Short-Term Debt \$ 123,000

Capital Leases 34,843

First Mortgage Bonds 100,000

Pollution Control Bonds 53,800

Spent Fuel Obligation _44,107

Total Debt 355,750 65.93%

Preferred Stock 36,500 6.76%

Common Equity 147,375 _27.31%

Total Capital \$ 539,625 100.00%

Q: Why is WMECO planning to retire some of its capital?

A: As approved in Docket 97-120, WMECO will sell its right to collect the RTC Charges which are associated with a substantial portion of its assets, which are referred to as the Transition Property. The right to collect the RTC Charges will be sold to a special purpose entity as part of the RRB Transaction, described in the Englander Testimony. Subsequently, those assets will be supported by the issued RRBs, not by WMECO's current capital structure, and the carrying cost of those assets will be the cost of the RRBs, not WMECO's cost of capital. The savings associated with this change in carrying costs is described in the Soderman Testimony. The WMECO existing capital which was supporting those assets before securitization is no longer needed for that purpose. Therefore the substantial reduction in WMECO's assets supported by its capital will be accompanied by a similar reduction in WMECO's non-RRB capitalization. Importantly, this reduction in capital will reduce WMECO's costs, which will produce additional savings for customers.

Q: How does reducing WMECO's total capitalization reduce costs?

A: WMECO will use a portion of the proceeds of the RRBs to retire debt and equity, thereby reducing or eliminating interest expense, preferred stock expense and equity return. These reduced costs translate into lower revenue requirements for WMECO, producing savings for customers.

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Q. Describe more specifically how much debt and equity WMECO expects to retire.

A. WMECO's current planned retirements are shown in Attachment 1 (Protected) to my testimony.

Q. What is the Company's methodology for determining the preference order of capital to be retired with RRB proceeds?

A. The Company's methodology is based on two goals. First, the Company should make progress toward achieving a solid investment grade capital structure as defined by credit rating agencies such as Standard and Poor's Ratings Services ("S&P") and Moody's Investors Service ("Moody's"). Second, the Company seeks to reduce its current cost of capital.

Q. What capital structure criteria do the credit rating agencies use in determining a solid investment grade capital structure?

A. One of the major factors rating agencies look at in determining a company's credit rating is the ratio of debt in the capital structure to total capital. If a company's capital structure is too debt-heavy, it is viewed as being more risky and consequently a lower credit rating will be assigned and the market cost of new capital will be higher. A higher cost of capital will produce higher rates for customers. Rating agencies currently target a capital structure of no more than 55%-60% debt to achieve a solid investment grade rating.

Q. In determining the ratio of debt to total capital, do the rating agencies calculate debt the same way that the Department does in its rate-making proceedings?

A. No. In traditional rate-making, WMECO's capital structure does not include short-term debt, capital leases or prior spent fuel obligations. Also, accounting rules and future ratemaking will require that the RRBs be reflected as debt on WMECO's balance sheet. However, for purposes of measuring WMECO's capital structure, the rating agencies include short-term debt, capital leases and prior spent fuel obligations as debt and exclude the RRBs.

Q. Why is achieving a solid investment grade rating important?

A. WMECO's credit rating is a factor in obtaining access to financial markets, determining rates and fees associated with the costs of obtaining working capital from banks and determining the cost of other financial transactions the Company may consider such as interest rate swaps, hedges or similar transactions. Improving access to financial markets and reducing future costs and fees reduces future revenue requirements.

Q. Is WMECO currently a solid investment grade rated company?

A. No. WMECO is currently rated BBB- by S&P and Baa3 by Moody's, the lowest level of investment grade. The Company seeks to raise its credit rating to at least BBB/Baa2, and believes it may be able to achieve ratings as high as BBB+/Baa1.

How will retiring WMECO's capital help obtain a solid investment grade credit rating?

A. Attachment 2 (Protected) to my testimony shows the impact on WMECO's capital structure as measured by rating agencies, at several different periods during the

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year, including the estimated pre-securitization level, post-securitization level, and projected balances at December 31, 2000. To summarize, the non-equity portion of WMECO's capital structure moves from approximately 72% pre-securitization to 66% post-securitization and to 63% at year-end 2000. Further earnings and debt retirement are expected to put the Company into the target range of 55% to 60% debt by mid-year 2001, and WMECO is expected to remain in that range thereafter.

Q. In what order of preference will the Company use proceeds to reduce the cost of capital?

A. First, WMECO will use proceeds to retire common equity, which is the most expensive form of capital. Common equity has a pre-tax rate of 11%; however, because equity is not tax deductible this rate needs to be "grossed up" for the effects of taxes that must be paid. Therefore, from a customer's perspective the current equivalent tax affected rate of common equity is approximately 18%. The Company cannot retire significantly more common equity than proposed in Attachments 1 and 2 without jeopardizing its credit ratings.

Second, WMECO will retire all of its preferred stock. Because the preferred stock dividends are not tax deductible, the effective rate on WMECO's preferred stock is approximately 12.6%. Retiring these securities, even with the inclusion of a call premium required by the terms of the preferred stock prospectuses, reduces WMECO's cost of capital more than retiring debt. Retiring all of the Company's preferred stock has the additional effect of removing a covenant restricting the amount of unsecured debt WMECO may have outstanding, thereby increasing the Company's financial flexibility.

The remaining proceeds will be used to retire debt. Details on the use of proceeds is shown in Attachments 1 and 2.

Q. Table 1, presented above, shows WMECO with over \$355 million of debt outstanding at the time RRBs are issued. How will WMECO determine which debt will be retired?

A. First, the Pollution Control Bonds and the Capital Lease are not callable and therefore cannot be retired. The interest rate on Prior Spent Nuclear Fuel is based on short term Treasury rates, which will always be lower than the interest rate on Short-Term Debt and is extremely unlikely to reach the level of the interest rates on First Mortgage Bonds of 7.375% to 7.75%, and therefore should not be retired. As a result, First Mortgage Bonds ("FMB") and Short Term Debt ("STD") have been identified by WMECO as the best candidates for retirement.

Q. How will the amount of each of these debt securities to be retired be determined?

A. The amount of each security retired will depend on market conditions at the time of the issuance of the RRBs and the impact of the retirement on WMECO's cost of capital. Under current market conditions, the Company would retire STD. The current STD interest rate of 7.625% is comparable to those of the FMB, and there is no related call premium, while there would be a call premium on the retirement of either of the FMB issues. This order of preference will be reexamined at the time of issuance and could be changed if interest rates have changed materially. Also, market conditions may enable WMECO to purchase FMB on the open market at costs below the call premium. The Company will be evaluating these opportunities if they occur.

Q. You stated that these capital retirements would reduce WMECO's Cost of Capital. Assuming the retirements as proposed, what is WMECO's new Cost of Capital?

A. The new Cost of Capital (including gross-up of cost of equity for taxes) would be

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12.36%, as shown in Exhibit RAS-2 to the Soderman Testimony. This is lower than the pre-securitization cost of 12.63% shown in the same exhibit.

Note that to the extent that FMB were to be retired instead of STD, the proportion of debt in the capital structure for rate making purposes would go down and the proportion of equity would go up. This would increase the composite cost of capital, which is not a desirable result. Thus the cost of capital impact will be considered in addition to relative interest rates in determining whether STD or FMB is retired with RRB proceeds.

Q. What is the expected weighted average interest rate of the RRBs?

A. At current market rates, the expected weighted average interest rate of the RRBs would be roughly 7.5%, assuming a AAA/Aaa rating is achieved.

Q. This rate on the RRBs is close to the interest rate on the debt you propose retiring. A relatively small increase in the RRB rate would make it higher than the interest on debt being retired. How can this benefit customers?

A. First, the RRB interest rate is not replacing the interest rate on the debt retired. As previously noted, the RRB rate replaces the Company's Cost of Capital on the assets securitized. Second, it must be remembered that the cost of future capital will depend on obtaining an improved credit rating, part of which will come from attaining a target capital structure of no more than 55%-60% debt. Leaving more debt outstanding would either jeopardize the target capital structure, and therefore WMECO's credit ratings, or require a reduction in the amount of costly equity being retired. Finally, retiring the combination of debt and equity as proposed does produce a lower cost of capital, providing savings for ratepayers.

V. STATUTORY REQUIREMENTS

Q: Please describe how WMECO's actions comply with the requirements of G.L.c. 164, §1G(d)(4) regarding the use of proceeds from the sale of RRBs?

A: Section 1G(d)(4) requires that WMECO establish, with the Department's approval, an order of preference for the use of RRB proceeds that will have the greatest impact on customer rates. Our use of proceeds as outlined above meets these criteria by targeting the highest cost securities consistent with reducing the cost of capital on a forward-going basis.

Q: What will NU do with the proceeds returned to it that represent previous equity investments in WMECO?

A: NU will use the proceeds for some combination of reduction in the number of shares outstanding through the repurchase of its common shares, payment of a dividend to its shareholders, or making investments consistent with its long-term strategy that will provide a return exceeding its cost of equity. NU needs to provide its (and indirectly WMECO's) investors an adequate return on their investments. These actions will contribute to achieving that return.

Q. Will all of the savings from the issuance of RRBs be passed on to WMECO's customers?

A. Yes. All savings of the proposed RRB Transaction will be passed through entirely to WMECO's customers and in no event shared with either NU or NU's shareholders.

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Q: Can you summarize your testimony?

A: Yes. The proposed reduction in capital structure and the preference order for the use of proceeds from the issuance of the RRBs will provide customer savings on an ongoing basis and satisfies the requirements of G.L. c. 164, §1G(d)(4). The two requested statutory waivers are essential for achieving these customer savings and should be approved.

Q: Does this conclude your testimony?

A: Yes.